No. 3983

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IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

SPOKANE & EASTERN TRUST COMPANY (a corporation),

Appellant,

vs.

UNITED STATES STEEL PRODUCTS COMPANY (a corporation),

Appellee.

BRIEF FOR APPELLEE

Upon Appeal from the United States District Court for the Eastern District of Washington, Southern Division.

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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Statement of the Case.

1. Introduction.

We shall follow the example of the appellant in the designation of the parties and shall likewise use round figures except when it is material to state the exact sum.

This action was instituted by the plaintiff, who is the appellee herein, United States Steel Products Company, a corporation of the State of New Jersey, to recover from the Spokane & Eastern Trust Company, a corporation of the State of Washington,

proceeds of a certain check belonging to the plaintiff. Central Bank & Trust Company, a banking corporation of the State of Washington, situated at Yakima and E. L. Farnsworth as Director of Taxation and Examination of the State of Washington, were also made defendants. The Central Bank was made a party defendant because of its trust relationship with plaintiff and its violation thereof.

E. L. Farnsworth, as Director of Taxation and Examination was made a party defendant because he was liquidating the Central Bank as an insolvent bank and under the statutes of the State of Washington was exercising the functions of a receiver (Session Laws of 1917, Chapter 80, Secs. 59 et. seq. p. 300; especially Sec. 62, p. 301 and Sec. 69, p. 304; Session Laws of 1919, p. 727; Session Laws of 1921, Chapter 7, Sec. 135, p. 68; Secs. 51, 52, 53, 54 and following sections; Session Laws of 1917, Chapter 80, Sec. 69, p. 304). Therefore, we shall hereafter refer to him as "receiver".

We call the Court's attention at the outset to the two following facts: (a) The plaintiff is not attempting to trace its property into the hands of the receiver of the insolvent bank. The claim as stated in the complaint and established by the evidence is that the proceeds of plaintiff's check did *not* come into the hands of the receiver. They were transmitted by the Central Bank at Yakima, to the Trust Company at Spokane, before the receiver took possession of the Central Bank. That this is the

theory of the plaintiff's case is shown by paragraphs V, VI, VII and VIII of the complaint (Trans. 4-7). (b) The receiver has not appealed from the judgment. Whatever effect the judgment may have upon him as a representative of the general creditors of the Central Bank, he accepts. He is not only contented and satisfied, but we have no doubt, gratified.

These facts eliminate from the case all questions which might be raised by the receiver as the representative of general creditors, e. g., the question of whether the proceeds of plaintiff's check augmented the assets in the hands of the receiver. In short, the judgment stands unchallenged either by the Central Bank or by the receiver. We call the Court's attention to these facts at the threshold because, if kept in mind, they will greatly simplify the future discussion of the case.

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2. The Admitted Facts.

A consecutive statement of the undisputed facts is requisite and necessary to a ready comprehension of the evidence relevant to the disputed questions of fact and should also facilitate the discussion and application of the legal principles involved.

Shortly prior to the 19th day of January, 1921, the Yakima Hardware Company, in payment of an indebtedness then owing by it to the plaintiff, United States Steel Products Company, mailed from

Yakima to the plaintiff's office at Seattle, its check for forty-seven thousand, nine hundred twenty-eight dollars and seventy-four cents ($47,928.74). We shall hereafter state this amount as $48,000. The plaintiff was at that time a customer and depositor of the Seattle National Bank at Seattle, and on the 19th day of January, 1921, it endorsed this check to the order of the Seattle National Bank and delivered the same to that Bank for collection and deposit to the credit of the plaintiff. The Seattle National Bank thereupon undertook the collection of the check for the account of the plaintiff. There was printed upon the face of the deposit slip upon which the deposit was entered, the following:

> "In receiving checks or other items on deposit payable elsewhere than in Seattle, this Bank assumes no responsibility for the failure of any of its direct or indirect collecting agents, and shall only be held liable when proceeds in actual funds or solvent credits shall have come into its possession. Under these conditions, items previously credited may be charged back to the depositor's account." (Par. III of Complaint, Tr. 2. Testimony, Townsan and Bray, Tr. 32).

Upon receipt of the check by the Seattle National Bank, it forwarded the same by mail for collection *and immediate returns* to the defendant Central Bank at Yakima. The check was not sent for credit. The letter of the Seattle National Bank transmitting the check to the Central Bank stated "We enclose for *returns* the following *cash items*" (Italics are ours). There were enclosed in the remittance

letter other items for collection which brought the total of the items so transmitted to fifty-one thousand, one hundred eighty-eight dollars and four cents ($51,188.04). (We shall hereafter state this amount as $50,000.) (See Par. IV of the Complaint, Tr. 3. Testimony, Miner, Tr. 33).

Not only was the check not remitted for credit, but the amount of the items so remitted was not charged by the Seattle National Bank to the Central Bank (See testimony of Miner, Tr. 34). Nor did the Central Bank credit upon its books the Seattle National Bank with the amount of the remittance. It was treated as a cash transaction (Testimony, of Lemon, Tr. 81). No relation of debtor or creditor arose. The check was received by the Central Bank some time before the morning of the 21st of January, presumably on the 20th of January too late to be presented (Testimony of Lemon, Tr. 35).

The Central Bank was not a member of the clearing house, but cleared through the Yakima Valley Bank, which was a member and acted as the clearing agent of the Central Bank. The check was presented through the clearing house to the Yakima Trust Company upon which it was drawn, and paid on January 21st.

There was presented through the clearing house at the same time the various other small items on various Yakima banks which had been remitted by the Seattle National Bank to the Central Bank for collection, and which went to make up the total

amount of the items of the remittance letter to $50,000. There were also presented through the clearing house in the same ~~letter~~ manner, various items held by the Central Bank against other banks in Yakima, aggregating approximately $7800. These items were checks which were drawn locally on local banks (Testimony of Lemon, Tr. 37). This brought the sum total of the items presented by the Central Bank to approximately $59,000.

There were presented at the same time through the clearing house, items against the Central Bank aggregating approximately $9,000, which were allowed. The balance in favor of the Central Bank was approximately $50,000.

In partial settlement of this balance, the Yakima Valley Bank, which had made the collections for the Central Bank as its agent, paid over to the Central Bank the sum of $48,000, retaining a small amount on deposit to the credit of the Central Bank (Testimony of Lemon, Tr. 36, 37, 38). This $48,000 so turned over by the Yakima Valley Bank to the Central Bank was in the form of two drafts, one for $45,000 drawn on the Bank of California at Tacoma and the other for $3000 drawn on the Fidelity National Bank of Spokane (Testimony of Lemon, Tr. 36). The Central Bank thus received the sum of $48,000, substantially all of which, as we shall later demonstrate, was the proceeds of plaintiff's check in transmissible form, i. e., in drafts. Yakima is located about midway between Seattle and Spokane; but instead of forwarding such proceeds di-

rectly west to the Seattle National Bank, the Central Bank transmitted the same in the opposite direction to the Trust Company at Spokane, at the same time transmitting a few cash items and notes amounting to about $4000 for re-discount, thus making a total charge of approximately $53,000 on that day against the Trust Company. The Central Bank then drew a draft on the Trust Company in favor of the Seattle National Bank for the full amount of the collection items received by it from the latter, to-wit, $51,188.04. All this happened on the 21st day of January, 1921.

On the next day, January 22nd, the Trust Company received said remittance including substantially all the proceeds of plaintiff's check and deposited the same to the credit of the Central Bank, collecting the $3000.00 draft on the same day at Spokane and the $45,000.00 draft at Tacoma on January 24th.

The draft in favor of the Seattle National Bank, issued on January 21st to effect returns on plaintiff's check, was not presented to the Trust Company until the 26th day of January. Prior to presentment of said last mentioned draft the Trust Company learned that the draft had been issued and was outstanding. With such knowledge and prior to presentment thereof, the Trust Company charged back to the Central Bank on its books certain overdue or otherwise bad rediscounts and other paper indorsed by the Central Bank, and undertook to absorb and apply all the proceeds of plaintiff's

check received by it to its indebtedness against the Central Bank. Consequently when the Seattle draft was presented on the 26th payment was refused, and on the subsequent demand of plaintiff to pay over the proceeds of the check so received by the Trust Company, payment of the whole, or any part thereof, was likewise refused (Tr. 11).

When the Seattle National Bank was advised of the non-payment of its draft, it charged back to the plaintiff the amount of the latter's check for which the Seattle National Bank had given its provisional credit, and the plaintiff has never received any return in money, or any returns whatever, on account of its check. (Testimony of Miner and Bray, Tr. 93).

It is expressly stipulated in the record that the Central Bank was insolvent during all the month of January, 1921, and part of the evidence on that feature of the case is omitted (Tr. 88). The Central Bank was closed by the Bank Examiner on January 27, 1921 (Tr. 58).

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3. The Controverted Questions of Fact.

In addition to the foregoing facts, the Court further found that both the Trust Company and the Central Bank were chargeable with knowledge of the Central Bank's insolvency and that the Trust Company was also chargeable with knowledge of plaintiff's ownership of the fund received by it.

These findings are assailed by appellant but are, in our opinion, conclusively established by abundant proof. The pertinent testimony will be summarized and discussed under appropriate headings in the argument.

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4. The Issues of Law.

Appellant also questions the trial court's conclusions of law, (1) that the Central Bank received and held the proceeds of plaintiff's check in trust, and (2) that the fund was traceable into the hands of the Trust Company.

Argument.

5. Outline of Subject Matter.

In answer to appellant's contentions plaintiff undertakes to support the decree upon the following grounds, in the order stated:

1. The title to the check remained in plaintiff and when collected the Central Bank received and held the proceeds thereof as agent or trustee for plaintiff (a) because such was the express understanding and agreement between plaintiff and the Central Bank, and (b) for the further and independent reason that the Central Bank was insolvent and consequently disabled from becoming a lawful debtor of plaintiff.

2. Appellant had full knowledge of plaintiff's rights and the insolvency of the Central Bank.

3. The identity of the proceeds was preserved as a fund and were traceable into the hands of the Trust Company.

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6. Title to Check and Proceeds Thereof Remained In Plaintiff by Virtue of Express Agreement.

Plaintiff's title to the check is not questioned. The cases cited to the next point are, however, specific and conclusive.

Appellant argues that upon collection title to the proceeds vested in the Central Bank. Our first answer to this contention is the express understanding and agreement of the parties. The capacity in which the Central Bank received and held the check depends upon the instructions contained in the letter of the Seattle Bank transmitting the same. By this letter the Central Bank is instructed that the check is transmitted for collection and returns, and it could, of course, accept collection on no other terms. The language of this letter is: "We enclose for *returns,* the following *cash items*" (Testimony of Miner, Tr. 33). In the banking business this language has a definite and certain meaning. It means that the recipient is not to credit the sender with the items sent for collection, but to collect and remit; and in fact, it was treated as a cash transaction by both banks. No charge was

made against the Central Bank by the Seattle Bank; likewise, no credit was ever given by the Central Bank to the Seattle Bank (Testimony of Miner, Tr. 34; testimony of Lemon, Tr. 81). Under such state of facts has been held almost unanimously that the proceeds of collection belong to plaintiff. The Federal Courts are unanimously for plaintiff.

> *Holder v. Western German Bank,* 136 Fed. 90, 68 C. C. A. (6th) 554: facts identical; check transmitted for collection and "remit New York Exchange"; holding collecting bank trustee of proceeds for owner, the court said: "The bank could not rid itself of that relation and became the mere debtor of the plaintiff by its own act. The trust was part of the plaintiff's security. Neither the plaintiff nor the Western German Bank, in his behalf, ever consented that the Florida bank should cast off the trust and become the plaintiff's debtor. It would be a most absurd consequence if a man in the possession, as an agent, of a fund belonging to another, could convert the fund into his own property by sending his check to the owner, and then, upon some change in his own circumstances, direct his bank not to pay it, and so transform himself into a debtor. Of course, if the owner consents to such a change of relationship between himself and his agent, or where the circumstances indicate that a credit in account is expected, which is the same thing, the result is different, because the destination of the fund is altered by agreement. But here there was no such agreement. The check was sent for collection and remittance. Satisfactory proof should be required that the owner assented to such change, in view of the consequences which would ensue. A man might be quite willing to trust another with the collection of his money when he would be very unwilling to loan it to

him. It would seriously impair the facilities for collecting commercial paper if it should be exposed to the hazards of conversion by the agent into whose hands the proceeds might come."

Titlow v. McCormick, 236 Fed. 209, 211; 149 C. C. A. (9th) 399; paper "received for collection"; owner not a customer with checking account and remittance implied; this court there held: "We regard it as clear that the relation of *cestui que trust* and trustee existed between the appellee and the appellant bank. In the similar case of American Can Company v. Williams, 178 Fed. 420, 422, 101 C. C. A. 634, 646, the Circuit Court of Appeals for the Second Circuit said: 'The relation of *cestui que trust* and trustee undoubtedly existed between the plaintiff and the Fredonia Bank. The bank violated every duty which it owed the plaintiff. The proceeds of the plaintiff's drafts held by it or its agents constituted trust funds which might be followed into the hands of the receiver, if they could be traced.' Authorities to this effect are so numerous as to make their citation unnecessary."

Macy v. Roedenbeck, 227 Fed. 346, 352; 142 C. C. A. (8th) 42; collection transmitted with instructions to remit "by draft", *held:* "It must be conceded that the relation of debtor and creditor never existed between Roedenbeck and the Bank of Sully. Roedenbeck was the owner of the note forwarded for collection and of the moneys collected, and it is clear that Roedenbeck could have obtained possession of the note at any time before its payment, or of the check, or of any moneys in the hands of the bank, received by the bank in payment of Roedenbeck's note."

Boone Co. Natl. Bank v. Latimer, 67 Fed. (C. Ct. W. D. Mo.) 27: paper transmitted for "collection and remittance"; proceeds a trust fund.

Clark Sparks etc. Co. v. Americus Natl. Bank, 230 Fed. (D. C. S. D. Ga.) 738: Identical facts; same holding.

The Decisions of each of the following states are exactly to the point:

(Ala.) *Hutchinson v. Nat'l. Bank of Commerce,* 41 So. 143: Transmissal with instructions to "remit in New York Exchange."

(Ark.) *State Nat'l. Bank v. First Nat'l. Bank,* 187 S. W. 673, 675; *held:* "The direction to remit immediately in Little Rock exchange shows unmistakably that the draft was sent for collection, and that there was no intention of the drawer to receive credit from the bank, but an expectation that the proceeds would be immediately forwarded, and the suggestion, remit in Little Rock exchange, was only to facilitate the receipt of the money."

(Ill.) *Nat'l. Life Ins. Co. v. Mather,* 118 Ill. App. 491, 494: forwarded for "collection and remittance".

(Ia.) *Messenger v. Carroll Tr. & Sav. Bank,* 187 N. W. 545: "collection and remittance".

(Kan.) *Kansas State Bank v. First State Bank,* 64 Pac. 634: "collection and remittance".

(Mich.) *Wallace v. Stone,* 65 N. W. 113: instructions to "collect and remit".

(Mo.) *German, etc. Ins. Co. v. Kimble,* 66 Mo. App. 370: "collection only".

(Neb.) *Griffin v. Chase,* 54 N. W. 572: sent for "collection and remittance".

(N. J.) *Thompson v. Gloucester City Sav. Inst.,* 8 Atl. 98: forwarded for "collection".

(N. Y.) *People v. Bank of Dansville,* 39 Hun. 187: facts identical; frequently approved by later New York cases.

(N. M.) *First Nat'l. Bank v. Dennis,* 146 Pac. 948: sent for "collection and remittance".

(S. D.) *Piano Mfg. Co. v. Auld,* 86 N. W. 21: transmissal for "collection and return".

(Tex.) *Contl. Natl. Bank v. Weems,* 6 S. W. 802: paper sent for "collection and returns". Leading case, frequently cited and approved.

(Wyo.) *Foster v. Rinker,* 35 Pac. 470.

Each and every one of these cases hold title to the proceeds of collection remains in the owner.

In order not to extend the brief but one decision is cited from each State. The cases could be multiplied indefinitely, but we deem it unnecessary. The net result of the reasoning and discussion of the authorities dealing with transactions identical with one in suit may be summarized as follows:

(a) When a bank consents to act as a collecting agent it assumes precisely the same duties and obligations toward its principal as an individual does

when he acts in the same capacity. In such cases no Court ever thought of discharging an individual from his trust relation because of a commingling of funds. If an attorney should remit the proceeds of a collection to his client by personal check or draft afterwards dishonored, no Court would stultify itself by deciding that the provisional acceptance of such check and presentment for payment would discharge the attorney of his trust relation and convert him into a simple debtor. Nor would it aid him to cite *Bowman v. Bank,* 9 Wash. 614, to the effect that the acceptance of a worthless draft or check operated as a payment or that the client purchased such check with the funds held by the attorney.

(b) The law governing the facts in suit is not to be confused with the law applicable to customers and depositors who assume with the bank the relation of an ordinary lender on time or on demand. In such cases the funds are deposited on the faith and general credit of the bank to be repaid subsequently, whereas, a remittance for collection and return is a strictly cash transaction without any intention of making a loan or even a sale or transfer to the collecting bank. Even if a cash sale or transfer were intended the result would be the same and would not be affected by an acceptance of the purchaser's draft or check, as it is universally held that no title passes where in such cases the paper received in lieu of cash payment is dishonored, as in this case.

(c) The trust relation as to the proceeds of collection is not destroyed *ab initio* by commingling or dissipation of the trust fund. Such conduct of the collecting agent may, however, eventually limit, or even defeat, the right to trace and recover the fund.

A practice or custom of commingling funds by a collection agent, however numerous its clients or complicated its business transactions, does not relieve it of its trust obligation. Banks solicit and transact an immense volume of business in conformity with the strictest fiduciary and confidential obligations, holding themselves out as "Trust" companies or trustees of the highest character, and are not at all inconvenienced by business complexities. It is, therefore, held in all the cases cited that the custom of banks to commingle funds in ordinary transactions will not be read into or regarded as part of an express agreement for collection and returns, like the one in suit.

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7. Appellant's Argument and Authorities on this Point.

It was argued by the appellant (Brief p. 42) that it could not have been intended that the Central Bank should remit to the Seattle Bank in specie. This we concede, but the point has no significance. In the cases already cited, particularly *Holder v. Bank* (6th C. C. A.); *Macy v. Roedenbeck* (8th C. C. A.); *Hutchinson v. Bank* (Ala.) and *State Bank*

v. National Bank (Ark.), the forwarding instructions to the collecting agent expressly required remittance to be made in drafts or exchange. In practically all the remaining cases cited the remittance was attempted exactly in accordance with the facts in suit. Such fact was in all the cases held in no wise to affect the trust relation.

It is further argued by the appellant that it must have been the intention of the parties that when the Central Bank had made the collection it should commingle the funds so collected with its own funds. This we do not concede. It may be that this is often done by collecting banks, but if they do they charge the whole of the commingled funds with the trust so long as the proceeds of the collection can be traced into them. The commingling of funds has no effect upon the relationship of the parties to each other. As decided in the cases cited such practice is pertinent only to the question of tracing and identifying the trust fund.

In this connection appellant relies on the case of *Commercial Bank v. Armstrong,* 148 U. S. 50. This case is clearly not in point, and has never been so considered by the Federal Courts, or in fact, by any Court except in *First Nat'l Bank v. Davis,* 19 S. E. (N. C.) 280, cited by appellant. The decision in that case was rendered in 1893 and was certainly not overlooked in the various Circuit Court of Appeal cases and other cases already cited. In the case of *Titlow v. McCormick,* supra, decided by this Court, that decision was used by the receiver

in support of the identical contention here made by appellant, but this Court there held that any custom of banks to commingle funds did not affect the trust relation involved in the handling of proceeds of collections. The same situation is undoubtedly true of the various State decisions rendered long subsequently to the Armstrong case.

In that case the Supreme Court called attention to the fact that the collection contract required settlement between the banks only periodically on the first, eleventh and twenty-first of each month, and therefore contemplated a time deposit either general or special. It also further concluded that "these collections were not to be placed on special deposit and held until the day for remitting", but were to be treated as a general deposit, and that the transmitting bank in that case was to be treated as a general depositor. There the transmitting bank gave its correspondent bank even greater rights than it would have had under the ordinary general deposit, in this, that the general depositor has the right to withdraw his deposit at any time on demand by check or draft, whereas, in that case a credit of ten days was expressly stipulated. Such express limitation of the transmitting bank's right to the funds necessarily implied the relation of debtor and creditor.

The statement of the Court in regard to commingling of funds, and the use of the deposit by the bank, was made argumentatively and not as a recital of the contract itself.

This branch of the decision in the Armstrong case was influenced by the further fact that the receiver against whom recovery was sought had not and would not come into possession of the funds sought to be recovered, because the proceeds of collection had been applied to the indebtedness of the failing bank by its sub-agent making collection; although the failing bank thus used and dissipated the proceeds they were never commingled in the true sense of the word.

Another branch of the case deals with the proceeds of collections made by sub-agents owing the failing bank and from whom the receiver had or would receive a balance. The receiver was held as trustee for the proceeds, and this upon the specific ground that title to such *proceeds* remained in the owner, notwithstanding the aforesaid "collection and credit" arrangement. In both instances the paper had been honored and paid. In neither instance had the actual proceeds ever been transmitted to the failing bank or in anywise reduced to actual possession; in both instances the sub-agents claimed title to the proceeds; in one instance offsetting against the failing bank's indebtedness, in the other crediting it with a balance. Obviously, the two branches of the case are logically opposed to each other. The net result of the decision would seem to be that the proceeds of collection remained a trust fund until the same were dissipated by the failing bank. Such was the reasoning of the trial court (39 Fed. 684). That branch of the case up-

holding the trust is the one most usually cited by the courts with favor (*Old Nat'l Bank v. German-American Natl. Bank,* 155 U. S. 556) and is certainly a strong authority in our behalf. If an arrangement for collection and credit would authorize or permit the original owner of the proceeds to recover the same after collection in the hands of a third party, the arrangement under consideration should certainly be sufficient to accomplish the same result, on the assumption that such third party took with knowledge.

In any event, the reasoning of Mr. Justice Brewer that it was the intention of the owner to extend credit certainly has no application to the facts in suit. As already pointed out the arrangement here was a cash transaction without any credit whatsoever. Plaintiff in this case, moreover, is not seeking to charge the receiver who never received the proceeds of this collection but is, on the contrary, pursuing the Trust Company because it did receive such proceeds with knowledge.

Appellant depends primarily on the Washington cases cited by it. The expressions of opinion found in these cases are undoubtedly influenced by the conclusion of those Courts that the commingling of trust funds with other property defeated a right of recovery. According to the view of those Courts at that time there could have been no recovery in those cases even had they held in favor of the trust fund. In any event, they are opposed to the great

mass and current weight of judicial authority, are illogical and unsound and should not be followed.

Appellant insists, notwithstanding, that this Court should feel bound by the early Washington decisions. It is very doubtful, however, whether even the Washington Supreme Court would feel itself compelled to follow *Bowman v. First Natl. Bank.* In the later case of *Hallam v. Tillinghast,* 52 Pac. 329, the Court concluded that it was not necessarily a contract but simply a presumption based on custom that the parties intended a credit relation, and likewise conceded that such presumption would not arise if the evidence showed a definite agreement between the parties. It is clear that a different arrangement was contemplated by the parties here.

Again, in the very recent case of *Raynor v. Scandinavian American Bank,* 210 Pac. 499, the Washington Supreme Court overruled its prior decision concerning the right to trace trust funds and aligned itself with the modern doctrine on the subject. True enough, as appellant says, this decision was rendered by a different department of the Supreme Court, but a majority of the department rendering the contrary previous decision concurred in overruling the same in this case. Hence, the authority of the early Washington cases must be regarded as considerably weakened even in that state.

8. Law Announced by Federal Courts Followed Regardless of Contrary State Decisions.

But it is immaterial what rule is adopted by the Courts of the State of Washington on this point, as it is a question of general commercial law upon which this Court will rule independently of state decisions and in accordance with the law as declared by the Federal Courts.

> *In Titlow v. McCormick, supra,* the early Washington cases were called to the attention of this Court on this very point but were disregarded.

> So, *in re Jarmulowsky,* 249 Fed. 319 C. C. A. (2nd), the Circuit Court of Appeals there held that it was not controlled by state decisions on the question as to whether or not title to a check deposited for collection passed to the bank (general deposit).

> *Oates v. Bank,* 100 U. S. 239, involving promissory note made and payable in Alabama; transaction entirely intrastate. *Held:* "Not bound by the decisions of those courts upon questions of general commercial law. Such is the established doctrine of this court, so frequently announced that we need only refer to a few of the leading cases bearing upon the subject".

> *Presidio County v. Noel Young Bond Co.,* 212 U. S. 58, refusing to follow the State Supreme Court decisions invalidating county bonds and upholding validity thereof on the grounds of general commercial law. Also refusing to be bound by State Court decisions as *res judicata.*

Supervisors v. Schenck, 72 U. S. 772, 784; County bonds held valid, notwithstanding contrary state decision.

Brooklyn, etc. Railroad Co. v. National Bank, 102 U. S. 14, affirming the rule in the Oates case.

Liverpool Steam Co. v. Phoenix Insurance Co., 129 U. S. 397, at page 443.

Swift v. Tyson, 16 *Peters 1,* the leading case.

Hamley v. Bancroft, 83 Fed. 444, (U. S. Circuit Court, California Morrow, Justice), declining to follow a decision of the state court as to the construction of a contract.

The cases cited by the appellant on page 50 of its brief in opposition to the above rulings are so clearly inapplicable to the case at bar that they need no comment.

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9. Relation of Creditor and Debtor Does Not Arise Under Any Collection Agreement Prior to Payment and Receipt of Actual Money.

In our discussion of the case heretofore we have proceeded upon the theory that the Central Bank had received the proceeds of plaintiff's check and we have so stated. And this is true in the sense that there had come into its hands the two drafts for $48,000 above referred to. But it had not completed the *collection* to the extent that it had, under any arrangement or understanding, the right to con-

sider itself as a debtor instead of an agent or trustee. It had not as yet, commingled the proceeds of the check with its own funds because it had not received any money which it could so commingle. The two drafts which it received, aggregating $48,000 were transmitted to the Trust Company and the latter completed the collection and received the funds. The larger draft of $45,000 was not paid until the 24th of January, which was the day before the Examiner, with the knowledge of the Trust Company, left Spokane for Yakima to close the Central Bank.

Never having received the proceeds of plaintiff's check in *actual money* capable of being commingled with its general assets, the Central Bank could not become the debtor instead of the agent of plaintiff under any of the cases, even those involving a collection arrangement providing expressly for a credit relation.

Armstrong v. National Bank of Boyertown, 14 S. W. (Ky.) 411, approved in Commercial Natl. Bank v. Armstrong, 148 U. S. 50.

Foster v. Rinker, 35 Pac. (Wyo) 470.

National Bank of Commerce v. Johnson, 89 N. W. 49.

Levi v. National Bank of Missouri, 15 Fed. Cases No. 8289.

Fifth National Bank v. Ashworth, 16 Atl. (Pa.) 596.

10. Debtor and Creditor Relation Under Any Collection Arrangement Prohibited by Central Bank's Insolvency.

The law that an insolvent bank has no right to accept the money of another on its general credit is now so thoroughly established as to require no discussion. This general rule is not questioned. Appellant contends, however, that plaintiff must be regarded as having become a general creditor of the Central Bank in the absence of proof and a finding that the Central Bank was insolvent of its own knowledge.

Under the facts in suit and the authorities already cited in support thereof, the finding of known insolvency is not essential to the existence and continuance of plaintiff's title to the proceeds of collection.

Even if plaintiff could under the facts be considered in the light of a general depositor proof of known insolvency does however support plaintiff's title to the proceeds of collection. So much is conceded by appellant.

The insolvency of the Central Bank is admitted but corporate and official knowledge is, however, disputed. The finding of such knowledge on the part of both the Central Bank and the Trust Company was, we think, cogently proved. In this connection we shall first summarize and review the testimony establishing knowledge of the Central Bank's insolvency on the part of its officers and agents.

11. The Central Bank had Complete Knowledge of Its Insolvency.

The following testimony does, we think, amply support the finding of knowledge on the part of the Central Bank, its officers and agents.

Insolvency during the whole of January, 1921, is admitted by appellant (Tr. 88). The following further admitted facts appear of record. In the latter part of December, 1920, and first few days of January, 1921, very heavy, in fact abnormal, withdrawals were made by depositors. In common parlance there was a "run" on the bank during the first few days of January (Ellis, Cashier, Tr. 94). The deposits in November, 1920, amounted to $665,000; on January 3rd, $513,000; on January 4th, $497,000 and on January 5th, $482,000, with a continual decrease thereafter at the rate of about $4,000 per day until on January 21st, $430,000; January 25th, $426,000 (Bank closed). (Tr. 84). Thus it appears the bank's credit and standing with local depositors had become greatly impaired, and that owing to general market conditions no improvement in deposits could be expected even if confidence were restored.

The foregoing conditions and a similar state of affairs during December, 1920, compelled the Central Bank to provide, for it, an enormous amount of cash. It therefore borrowed $50,000 on bills payable secured by Liberty Bonds. Although this was the legal limit of borrowing by such means (Sec. 3261

Rem. Comp. St.) it was but a drop in the bucket. Collections were so inadequate that prior to the first of January the Bank had been compelled to rediscount $31,000 of its bills receivable with the National City Bank at Seattle and $114,000 with the Trust Company. The $200,000 thus provided proved wholly inadequate to meet the exigencies of the situation, and in the early days of January it became necessary to create an overdraft of more than $50,000 with the Trust Company (Tr. 87). Its statutory cash reserve had become a minus quantity. The small per cent of cash reserve shown by the books consisted almost wholly of dishonored paper fictitiously carried as cash, and if correctly entered would have shown an additional indebtedness of about $8000. The only possible resource left was through the collection and rediscount of its bills payable, already somewhat depleted and "slowed down" through meeting the withdrawal of about $150,000 deposits during the month of December.

Out of this note pouch the bank and its officials were under the dire and compelling necessity of promptly meeting a sudden loss of more than $50,000 in deposits during the first three or four days of January, and were, moreover, face to face with the absolutely certain further decline of deposits at the rate of approximately $4000 a day. They were also required to cover dishonored and past due fruit and produce drafts amounting to more than $8000 and in addition they were required to meet and cover a constantly maturing contingent liability on

the $145,000 rediscounted notes. In other words, they were required to use the note pouch to cancel without delay an indebtedness exceeding $60,000 and were, moreover, compelled to provide a further sum in excess of $4000 per day in order to keep afloat.

In the face of such imminent peril and impending disaster, can it be believed that the note pouch of the bank was not a matter of serious and grave concern on the part of the officials in charge? Can it be doubted for a moment that it received the most careful and painstaking attention, that it was the object of long and searching investigation, and that the value of the collateral, if any, and the financial condition of the borrowers and their ability to pay was not most thoroughly canvassed and very carefully appraised?

There was nothing peculiar about the bank's paper which would make its valuation and appraisement difficult. The testimony is undisputed that the credit men of the other Yakima Banks were easily able from their general knowledge, and upon a single day's investigation, to appraise accurately the bank's bills receivable and say for a certainty that more than $100,000 of such paper was totally valueless and the remainder of such doubtful value that the bank could not liquidate for more than thirty per cent of its indebtedness (Tr. 66, 78, 79, 131). That such knowledge was not uncertain or mere guesswork is established in the light of subsequent events, as appears from the testimony of the liqui-

dator, based on developments a year later that the assets would not realize to exceed thirty-five or forty per cent of the indebtedness (Tr. 99).

Appellant (Brief p. 62) admits that the bank's officials had full knowledge of all things concerning its financial condition, save one, that they did not know of the doubtful quality of the paper until the very last, when they were advised by the Yakima bankers that much of it was utterly bad. Although a large part of the loans had been negotiated by the bank's then acting officials, and the remainder had been frequently renewed; regardless of the further fact that such officials had been in constant and daily contact with the note pouch, devoting practically all their time and attention to securing financial statements and history sheets of the various borrowers for the purpose of negotiating rediscounts; and, in the face of the fact that they had been strenuously endeavoring to force collections to the very limit in order to meet the enormously pressing and severe needs of the bank for ready cash; still, appellant questions the knowledge of these officials as to the true value of the bank's paper until they were so advised.

Let us examine the knowledge of the parties handling the note pouch a little more in detail. Mr. Buchholtz who had charge of the note pouch from the 6th until the 25th of January, and Mr. Triplett of the Trust Company in Spokane, disclose adequate knowledge of the subject in their correspondence. In the letter of January 6th (Tr. 142),

Buchholtz offers Franc Investment note $11,000 endorsed by Mr. Barghoorn, president of the bank, and further endorsed by the bank without recourse, saying:

> "Don't swear; I figure that you are not banking on the Central Bank endorsement anyway. You have got an overdraft and will have."

To this Triplett replies, January 8th (Tr. 145),

> "We have great confidence in your ability to pick out the kind of notes we want and will ask you to work along those lines instead of asking us to take the Franc note. I did my darndest to put it over for you, but the powers that be could not see me for dust."

Letter, Buchholtz, January 7th (Tr. 143) offers for rediscount insurance premium notes ranging from $50 to $225.00 with comment "Don't swear, I'm trying this out to see what you think of it". Letter, Triplett, January 14th (Tr. 168): "We all feel there is going to be a good sized loss on Small", one of the bank's borrowers, owing $16,250 exclusive of liability on dishonored fruit drafts (Tr. 182) "Our people aren't satisfied with the Small notes. They think he is broke" (Tr. 226). Letter, Triplett, January 15th (Tr. 172), questioning the quality of certain notes. Letter, Buchholtz, January 18th (Tr. 192), sending two little but good notes says, "I wish I had about $20,000 of stuff like this", indicating positively that he had not and remarking "Don't laugh, every little helps, you know". Letter Buchholtz, January 19th (Tr. 193), submitting poor note for collateral saying, necessary to do so

from time to time as substitute for notes collected, and proceeds held by Central Bank. Letter Buchholtz, January 19th (Tr. 194) $2500 note withdrawn from collateral to bills payable and rediscounted, indicating absence of good paper in note pouch. Letter Buchholtz, January 19th (Tr. 198), admitting impropriety of not charging up unpaid rediscount at maturity, saying:

> "It is rotten but for the present no doubt for some weeks it will remain a question of which is preferable to you, over drafts or past due rediscounts. I would like to increase our rediscounts about $20,000 and get a balance enough ahead to cover charges of maturities, but would you consider stuff that would not be paid until the 1921 crop returns are in?"

thus indicating the only quality of paper available for rediscount. Such paper can certainly be characterized as "slow", but judged by the results of 1920, it certainly could not be described as "good". Letter Triplett, January 20th (Tr. 201), questioning value of note. Letter Triplett, January 20th (Tr. 203), discussing value of paper substituted as collateral saying, "I noticed you don't say *security*. Merely use the word 'collateral'. Nuf sed. However, there are some things we have to make the best of". Letter Triplett, January 20th (Tr. 204), summarizing general conditions adversely affecting value of the bank's paper. Letter Triplett, January 21st (Tr. 208), condemning note offered as collateral substituted for note withdrawn for rediscount, condemning it as utterly worthless, but accept-

ing same, thus indicating belief that nothing better could be had. Letter Triplett, January 21st (Tr. 209), accepting for rediscount note of questionable value, thus indicating knowledge that nothing better could be obtained; finally Letter Buchholtz, January 21st (Tr. 219) saying,

> "At present practically all of the paper which I have nerve enough to send for rediscount is there, with the exception of a small amount in the process of collection or renewal, and some miscellaneous small stuff on which we haven't statements and information",

thus clearly indicating the possession of statements and information on all paper except "some miscellaneous small stuff", undoubtedly the very information enabling the other Yakima bankers to appraise the paper quickly.

Thus it appears that Buchholtz, in full charge of the note pouch for the Central Bank and, as plaintiff contends, also for the Trust Company, was, on the 21st day of January, the very day plaintiff's check was collected, possessed of complete knowledge that all the Central Bank's paper which could possibly be considered fit for rediscount had already been negotiated and that the Central Bank was without any resources whatsoever to meet the daily withdrawal of its deposits or satisfy its $16,000 overdraft (Tr. 87).

Buchholtz, true to form, says these statements refer only to the liquidity and not to intrinsic value. What about the Small item alone, notes $16,250, overdraft $1900 (Tr. 182) and stranded fruit drafts

$10,000 (Tr. 210, 233), total $28,000.00? Some of this paper had been rediscounted, presumably on the assumption that it was better than the remainder of the note pouch. The idea that Buchholtz could not and did not appraise the bank's paper accurately is simply preposterous. Checking up country banks was his business; he knew the game; he was "one of our right hand men"; "we considered him our *prize* man" (Tr. 52, 104, 121).

The indisputable knowledge of Buchholtz is clearly imputable to the bank. The mere fact that he had not been given an official title is of no consequence. He was in complete charge of the credit department and had full authority in the matter of collections and rediscounts. In other words, he was in full and complete control of the most essential function of the bank at that time and was not subject to the authority of the cashier (Testimony of Barghoorn, president, Tr. 49, 51, Ellis, Cashier, Tr. 97; letter Buchholtz, Tr. 184-191). He was the whole show with Ellis on the job for effect (Tr. 126, 190).

The point urged by appellant that he was without authority to close the bank is immaterial. Although such power lies solely with the Board of Directors, it is, nevertheless, universally held that knowledge of an agent in charge of corporate affairs acquired in the course of duty is imputed to his principal. Extended citation of authority is unnecessary. *Clark etc. v. Americus Natl. Bank,* 230 Fed. 738, is a good example. In that case, knowledge of insolvency on the part of an assistant cashier was imputed to the

bank. Again, in *Pennington v. Third Natl. Bank,* 777 S. E. (Va.) 455, the cashier's knowledge of insolvency caused solely by his embezzlement and unknown to the directors was imputed to the bank.

Mr. Ellis, the cashier, must also be held to have been in possession of full knowledge of the bank's financial condition for the reasons already stated. There is nothing whatsoever in the record to justify a contrary conclusion. Appellant misinterprets his testimony concerning his knowledge. The statement that he had not had an opportunity to make himself acquainted with the quality and value of the bank's loans referred solely to his knowledge in June, 1920, when the Bank Examiner made his examination and criticised his methods (Tr. 97). He had then been with the bank only a short time (Tr. 93). His testimony is totally devoid of any assertion on his part that he was not fully advised in January, 1921, more than six months afterwards. Any optimism he may have had did not limit his knowledge; it merely indicates the use he may have made of it. The essential question to be determined is whether he was in possession of the facts. His general intelligence and experience in the banking business are not questioned or criticised, and even if not up to standard it is impossible to believe that he had not learned in the course of his duty extending over many months what the other Yakima bankers were able to ascertain and definitely determine within a few hours. He was, of course, the subject of criticism by the Trust Company because he did not send

satisfactory rediscounts. The correspondence already reviewed shows that Buchholtz could do no better. The efforts of both were the subject of ridicule, one hostile, the other friendly. The ability of Buchholtz is not questioned. It would, therefore, appear that the failure of Ellis was not due to want of capacity but to the force of adverse circumstances. His intelligence and knowledge can hardly be questioned because he defended himself with a little optimistic boosting or trader's talk in the matter of rediscounts. Some men have a sense of loyalty to the institutions they serve and every one objects to adverse criticism. Naturally he expressed the brighter side. He does not disclaim knowledge but merely denies responsibility on the ground that the bad loans were not of his making, and that the financial condition of the bank was a matter beyond the remedial powers of himself, or anyone else, i. e. that a large part of the bank's paper was worthless when he joined the institution, and such undoubtedly is the fact.

As already appears, Buchholtz, a stranger in Yakima, readily satisfied himself of the bank's insolvency in a very short space of time. It is inconceivable that he did not communicate his findings and knowledge to Ellis. The evidence is conclusive that he did so, and that he did moreover insist that Ellis should govern his conduct accordingly (Tr. 95, 184-191).

So far as Barghoorn, the president, and the other directors are concerned it is a plain case of "ab-

sentee landlordism". Barghoorn, after pledging his assets to the Trust Company to cover his personal indebtedness and guaranteeing that of the bank, practically surrendered any voice or control that he may ever have exercised and left the bank to its fate in the hands of the Trust Company. Mr. Ross, the vice-president, and a director, but had nothing to do with the bank, knew the situation (Tr. 67). He did understand the situation (Tr. 144, 166). As said by Buchholtz, the bank was "a ship without a captain" (Tr. 153). Ellis and Buchholtz were, therefore, the only corporate agents actually in charge.

There can be no doubt that knowledge on the part of Ellis and Buchholtz is conclusively established.

Exposure to facts or means of knowledge constitutes proof thereof (*In re Silver,* 208 Fed. 797):

> "When we say that a person has knowledge of an existing condition we mean that his relations to it, his association with it, his control over it, his direction of it are such as to give him actual, personal information concerning it" (*Parrish v. Commonwealth,* 125 S. W. (Ky.) 339, 347).

Knowledge far less than that shown on the part of these agents has been held to support a finding of known insolvency. Even in the absence of proof of actual knowledge such as is here presented, it has frequently been held that knowledge of the bank's

financial condition on the part of its active officials will be presumed.

> *Clark etc. Co. v. Am. Natl. Bank,* 230 Fed. 738.

In *State v. Welty*, 118 Pac. (Wash.) 9, 15, it is said that

> "if, by the exercise of such (reasonable) diligence in making an examination and inquiry in respect to the solvency or insolvency of the bank, its true condition could have been discovered, then, under such circumstances, the presumption will be that they had knowledge" (citing cases).
>
> *State v. Quackenbush,* 108 N. W. (Minn.) 953, 957.

A reckless indifference or neglect will not be inferred to overcome such presumption. By continuing business the Central Bank and its officials made active representations of its solvency, and, as has been shown, the actual contrary fact was within their easy means of knowledge.

> "If the fact be one within his easy means of knowledge and he have no knowledge of the fact a jury would be authorized to believe that the statement was knowingly false" *(Hindman v. First National Bank,* 112 Fed. 931, 944; 50 C. C. A. (6th) 623).

In that case Judge Lurton quotes the following from the leading English authority on the subject:

> "Although means of knowledge are * * * a very different thing from knowledge, if I thought that a person making a false statement had shut his eyes to the facts, or purposely ab-

> stained from inquiring into them, I should hold that honest belief was absent, and that he was just as fraudulent as if he had knowingly stated that which was false" *(Derry v. Peek,* 14 App. Cas. 337, 375).
>
> In *Nevada Bank v. Portland Natl. Bank,* 59 Fed. 338 (Gilbert J.) dealing with a representation as to the solvency of a third party, it is said: "By the weight of modern authority it is held that the law imputes an intention to deceive in every case where one recklessly asserts that to be true which is untrue and concerning which he pretends to have a knowledge which he has not (citing cases). Of this class is the cause of action contained in the second count of the complaint. It is there alleged that the representations were false; that they were made for the purpose of gaining credit for the Ainslie Lumber Company; that they were negligently and carelessly made, without examination or investigation; that, if investigation had been made, the untruth of the facts represented would have been made apparent. These allegations sufficiently state a cause of action." (Fraud and deceit.)

Under the facts and the law the Central Bank's knowledge of insolvency is, we think, conclusively established.

With full and complete knowledge of its hopeless insolvency, it was the duty of the Central Bank to close its doors and in failing to do so was guilty of fraud. Whatever may have been the right and privilege of insolvent banks in past years to continue operations in the forlorn hope of ultimate rehabilitation they are now required under present

federal and state legislation to transact business in a safe manner and in full compliance with statutory prohibition against inviting credit and consequent loss when insolvent. Although banks and their officials are not required to know the solvency of their institutions at their criminal peril,

> "Safety is secured by requiring officers having the control or management of banks to keep closely in touch with the assets, and to have a reasonable knowledge of their value, and to refuse to receive deposits when they find they are not amply sufficient to pay all debts exclusive of capital stock, surplus, and undivided profits of stockholders. If a bank continues to do business when it is not solvent in this sense, and it receives deposits, it is guilty of negligence of so hazardous a character as to amount to positive fraud and criminal liability under the statute" *(Gass v. State,* 172 S. W. (Tenn.) 305, 309-10).

> "Under the statute the bank has no right to continue business when its officers know, or have good reason to know, that it is unsafe or insolvent. If it does continue business, then the intent to cheat and defraud whoever deals with it irresistibly arises. The dishonest purpose comes from the knowledge of the officers, extends to all persons having dealings with the bank, and it is immaterial whether there was or was not a distinct intent to cheat or defraud a particular customer; otherwise, the bank might hide behind the alleged *bonafides* of the official and the very purpose of the statute be defeated" *(Hyland v. Roe,* 87 N. W. (Wis.) 252, 253).

There is no use to discuss any hopes of recovery. On the very day plaintiff's check was collected,

Buchholtz likened himself unto a physician at the bedside of a dying patient. His bulletin reports immediate death and dismisses chances for recovery as well meant consolation talk for the mourning family (Tr. 221). Can the Central Bank's certain and absolute knowledge of its insolvency be doubted?

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12. Appellant had Full Knowledge of the Central Bank's Insolvency Through its Agent There.

The knowledge of Mr. Rutter, president of the Trust Company, and of Mr. Triplett, vice-president, is conceded to be binding on appellant. It does, however, disclaim the relationship of principal and agent so far as the knowledge of Mr. Buchholtz is concerned. That he was at all times the agent and representative of the Trust Company is, we think, fully established by the proof.

Mr. Buchholtz entered the employment of the Trust Company in the early part of 1914, and has so continued, with certain interruptions, most of which were brief, up to the present time (Tr. 125, et seq.). True enough some of the witnesses testified that the relations between the Trust Company and Mr. Buchholtz were severed when he left for Yakima. We are of opinion, however, that such statements are to be regarded as mere conclusions of the witnesses instead of an accurate statement of the actual facts. Mr. Rutter and Mr. Triplett did, however, testify that they valued Mr. Buchholtz very highly and were sorry to lose him, but that they

took into consideration his welfare and recommended him for the place as they thought

> "it might be a good thing for him as it looked at that time as if the Central Bank was *a nice opportunity for a young man* in a growing town like Yakima" (Tr. 101).

The unimpeachable facts completely nullify this testimony.

The relations of the two banks were very close indeed. Mr. Barghoorn had been a director of the Trust Company since 1908, but found his finances in such condition that he had been compelled to pledge the best of his assets to the Trust Company to cover the indebtedness of himself and his bank (Tr. 138). The Central Bank was, moreover, a very small institution with a capital stock of only $50,000 and was then indebted to the Trust Company on bills payable and rediscounts in the sum of $142,000. At that time it had been suffering a severe run on its deposits and had accumulated a large overdraft with the Trust Company (See evidence, supra). Mr. Ellis was right then in communication with Mr. Barghoorn concerning the bank's predicament (Tr. 94).

The consultations between Mr. Barghoorn, Mr. Rutter, Mr. Triplett and Mr. Buchholtz with reference to Buchholtz' going to Yakima, occurred on the 5th day of January, at about 5 o'clock P. M. There is no evidence that the matter was ever broached before. The decision that he should go was arrived at instantly. In one hour and one-

half from that time Buchholtz's grip was packed and he was on the train for Yakima (Tr. 133). On the same day Mr. Triplett, vice-president of the Trust Company, wrote Mr. Ellis, the cashier of the Central Bank, a letter in which, after referring to certain notes held by the Trust Company for rediscounts as unsatisfactory said,

> "but as Mr. Buchholtz who is one of *our right hand men* (italics ours) is accompanying Mr. Barghoorn tonight, he will endeavor to obtain substitution of other paper" (Tr. 115-116-52).

When Mr. Triplett gave this testimony he had evidently forgotten this letter and the only explanation he could offer on cross examination was that "we had not yet gotten to the place where we realized he was gone". It was not stated when they did get to the place where they did realize it.

Notwithstanding the protestations of Mr. Triplett and Mr. Rutter, Buchholtz wrote a letter to Mr. Triplett on the 10th of January, five days after his arrival in Yakima, in which he says:

> "To assist Mr. Blake in checking up collateral, the following is now in my possession as *agent for the Spokane & Eastern Trust Company*" (italics ours).

Then follows a list of notes (Tr. 154).

After Buchholtz' arrival in Yakima he carried on a voluminous correspondence with the officers of the Trust Company in Spokane, conveying to them the most detailed information, some of it of an intimate and private character, not only of the condition

of the Central Bank, but his relations and experiences with the other employees. These letters are all set forth in the record from pages 142 to 237. Yet, during that entire period, he did not write a single letter to Mr. Barghoorn, who lived in Spokane and was absent from Yakima during the entire period except for a few days (Tr. 51,117). Does this look as if he was representing Barghoorn alone, and not at all the Trust Company?

His employment was never authorized by the Board of Directors of the Central Bank (Tr. 94), and the liquidator of the bank has refused to allow his salary, claiming that he was not an employee of the Central Bank (Tr. 116).

The very first day after his arrival at Yakima, he sent to the Trust Company a note for $11,000 upon which Sikko Barghoorn (to whom he refers as S. B.) for rediscount, and says that he is doing this on his "own initiative and not at the request or suggestion of S. B. or anyone else". Notwithstanding the fact that S. B. was then in Yakima, as shown by his letter of the next day (Tr. 145).

Having referred now to the first letter, we next invite attention to the next to the last letter which Buchholtz wrote. This letter is dated the 24th of January, 1921, and is addressed to Mr. Triplett, the last sentence of which is, "You see I don't know just how far you can go on S. B. and since he has resigned from the Board (of the Trust Co.), it must be down to a clean-cut proposition" (Tr. 237). Does this sound as if he were representing S. B.?

It was testified, as pointed out by the appellant, that complaints were made by the State Banking Department to Barghoorn concerning Ellis, his cashier; that Barghoorn had been urged to make a change in this office and had finally concluded that eventually he would have to do so; that the Trust Company was not satisfied with the way Mr. Ellis was handling the re-discounts which they sent to the Central Bank; that Mr. Buchholtz was hired by Barghoorn to go to Yakima and take charge of the selection of the rediscounts, acting in that capacity solely as the agent of the Central Bank; that it was contemplated that eventually he would succeed Mr. Ellis as cashier; that they thought this presented a fine business opportunity to Mr. Buchholtz—and so forth; and that these were the only reasons for Mr. Buchholtz leaving Spokane and going to Yakima into the Central Bank.

It is possible that there may have been in the minds of some of them the possibility that Buchholtz might be given the office of temporary cashier until Barghoorn might find another acceptable man to take the office permanently. This would have been in line with Buchholtz' previous activities. But to be asked to believe that Mr. Buchholtz left the Trust Company for the Central Bank to avail himself of "a fine opportunity for a young man", while a run was on, and the very life of the Central Bank was trembling in the balance; and in

view of the fact that the matter was first broached at five o'clock on the day he left; and that he was on the train at 6:30 that night, was too severe a tax upon the credulity of the trial Court.

It may be true that after the 5th of January, Buchholtz was no longer on the payroll of the Trust Company, but this fact is not significant; for when a large bank sends its outside "doctor" to take charge of one of its failing "patients", it rightfully makes the "patient" pay the expense. As Buchholtz puts it, the Trust Company was "relieved of his salary" (Tr. 160).

An "outside doctor" is what Buchholtz really was. One cannot read his own evidence and come to any other conclusion (Tr. 125).

The larger banks have their outside men who are kept for the purpose of taking charge of emergency cases such as that of the Central Bank. He himself told Mr. Miner that he was the outside man for the Spokane & Eastern Trust Company (Tr. 72); and introduced himself to Miner by presenting his card in which he described himself as being in the "Credit Department of the Spokane & Eastern Trust Company"; and he so introduced himself to Mr. Louden, cashier of the First National Bank of Yakima. This conversation with Louden took place shortly before the failure of the Central Bank. Buchholtz introduced himself as a "representative of the Trust Company"; stated that he was "looking after some affairs of the Trust Company" and that he had

just finished a similar job in the northern part of the State (Testimony of Louden, Tr. 80).

On January 9th Buchholtz wrote to Rutter in which, after asking Mr. Rutter to use his influence with State Banking Department to keep the examiners away, gave as his reasons for such request that customers would see them at work and possibly start withdrawals, and says: "As for myself. No one has gotten curious,—I am a new man working in here in Van's place, who just left the first". Van was one of the former assistant cashiers of the Central Bank (Tr. 95). Buchholtz is thus congratulating himself that no one has as yet discovered that he is there, practically in charge of the bank for the Trust Company.

We say practically in charge, for in his letter of January the 18th to Mr. Triplett he gives an account of how he had it out with Ellis as to who was boss (Tr. p. 184) and at the same time as to why he had been sent to take charge. He writes:

> "To end our argument and conversation we both agreed that it was desirable that he stay on the job for effect, and I added that I hoped strongly that the prospective purchasers would buy the institution and bring enough deposits to take up all indebtedness *and clean up with the S. & E.* and stay out and that as the new people had expressed a desire to have him remain with them I wished him and the bank every possible success in the world, but in the meantime, while I was here, there was no sense in the bank paying my salary and *heavy expense* if he was going to pull any more stunts over me like this one; that I had lots of other work that

> I could do and didn't need this job as far as I was concerned, *but that I had been sent here to help liquidate and that results were expected of me* and I wouldn't stay without his recognition and cooperation. As he expressed it, 'ripped him up pretty severely', but Ellis finally promised that he would see nothing of importance was done over my head again."

In answer to this letter Triplett commends him and especially Buchholtz' insistence that the policies of the Directors be disregarded, and he says:

> "The kind of business you should support now is that of *non-borrowers* who will have crops and *whose deposits can be used to liquidate indebtedness"* (Italics ours) (Tr. 213).

These letters, together with that of January 9th, disclose the true situation, i. e. that Buchholtz had been sent to Yakima because of the heavy indebtedness of the bank to the Trust Company and of the run upon the bank; he had been sent to help liquidate the indebtedness of the bank to the Trust Company. And, fortunately, we are not required to conjecture and surmise as to who imposed this task upon him or whom he represented in the matter. In his letter of the 23rd of January addressed to Mr. Rutter he says:

> "It is by far the most stupendous task *you* have ever seen fit to put me to" (Tr. 231).

Ellis, the cashier of the Central Bank, says:

> "That the occasion for his (Buchholtz) coming was that on the beginning of the new year, on the 3rd of January, there were abnormal con-

> ditions in the bank; very heavy withdrawals, and he (Ellis) communicated with Mr. Barghoorn, and Barghoorn came down with Buchholtz on the night of the 5th of January. There had been something of a run on the bank during the first two or three days of January" (Tr. 94).

It seems from the correspondence that Buchholtz had exercised the right to make substitutions of collateral which he held as agent for the Trust Company, withdrawing such of the bills receivable of the Central Bank for that purpose as he chose (See letter of January 19th, Tr. 194); and this is in harmony with the testimony of Mr. Lemon, the assistant cashier of the Central Bank, who testified that Buchholtz had to do with the renewing of notes, securing of collateral, financial statements, and *had to do with the note pouch* in general (Tr. 82). And it was in harmony with the testimony of Mr. Ellis to the effect that Buchholtz had unrestricted access to all the securities (Tr. 95), and that he and Buchholtz jointly had charge of the Credit Department (Tr. 97).

Triplett, in his letter to Buchholtz of January 20th, says:

> "We are looking to you to keep us using black ink instead of red" (Tr. 204).

In another letter of January 9th addressed to Mr. Triplett Buchholtz urges him to write, and adds "I like to hear from headquarters" (Tr. 151). And in another letter to Triplett on the 14th he says:

"Keep writing me. It's great to hear from home" (Tr. 170).

The evidence shows that Barghoorn was trying to sell the bank and that if the sale was made Ellis would remain cashier (See Buchholtz' letter of January 18th, Tr. 190). Now it is quite clear that if the officers of the Trust Company got him the job in the Central Bank because they thought it was "a nice opportunity for a young man" to succeed Mr. Ellis as cashier, as Mr. Triplett testified, they would not at the same time be exerting themselves to the utmost to effect a sale which would prevent Mr. Buchholtz from availing himself of that "nice opportunity". And yet Mr. Buchholtz wrote to Mr. Triplett on January 7th, the second day after his arrival in Yakima in which he says:

> "We will know in a day or two if the sale matter goes through. They are going to get together tomorrow P. M. S. B. (Sikko Barghoorn) will leave for Spokane tomorrow night unless they ask that he stay, although he has given Ellis power to close deal."

Again Mr. Buchholtz, in his letter to Mr. Rutter of January 9th, says:

> *"We, of course, all hope to make the sale* and Mr. Ellis is firmly convinced it will go through, but not depending on that and the benefits to be derived immediately, we face the task of liquidation to the limit" (Italics ours) (Tr. 148).

Buchholtz, in his letter to Triplett of the 10th of January, says: that he intends to cut down the force

"if it turns out that no sale is made and I am to remain here very long" (Tr. 153). Triplett, in his letter of January 24th to Buchholtz, urged that the deal for the sale of the bank "should be hurried along as fast as possible"; and added, "If conditions go on much longer as they are now the institution will soon be in a place where no one will purchase and then it is a case of either closing its doors or getting someone to see it through" (Tr. 226).

In addition to the correspondence already considered further evidence of Buchholtz' agency for the Trust Company is found in the testimony of Mr. Hay, Bank Examiner, who testified to a conversation which took place at a meeting of the State Guaranty Board on January 22nd. The Governor had become aware of a Bradstreet report to the effect that the Central Bank had suspended payment and had requested witness to send an examiner to the Central Bank. At this meeting the Governor inquired of the witness whether an examination of the Central Bank had been made and upon receiving a negative answer insisted very forcibly that it must be done at once. Whereupon Mr. Rutter asked the Governor not to act too hastily, saying:

> "We have a man over there who is looking after things, and things are coming along very nicely" (Tr. 69-70).

Here we have one statement at least of the President of the Trust Company in harmony with the correspondence showing fully the nature of Buch-

holtz' agency and the purpose on the part of the Trust Company to forestall any interference with its liquidation of the Central Bank.

The testimony of Mr. Triplett concerning the re-employment of Buchholtz by the Trust Company after the Central Bank had been closed, should not, we think, pass unnoticed. When the Bank Examiner took charge of the Central Bank, Buchholtz removed certain paper from the bank and made affidavit that the same belonged to the Trust Company and was under his personal control. The Examiner telephoned the Trust Company and was advised that the notes in question belonged to it (Tr. 59) and were of course rightfully in Buchholtz' possession as its agent (Tr. 154). Mr. Triplett, nevertheless, testifies to the following conversation as to re-employment:

> "I called him up and he said 'the Bank is closed'. And I said to him that I supposed he was foot loose, and he said 'yes'. I said that I had a job for him; that I wanted him to take possession of all the notes and collateral we had down there and look after our interests in Yakima" (Tr. 103).

This to an admitted agent already in possession and for a long time past in the full and active performance of that very duty. "Supposed he was foot-loose; had a job for him;" Such testimony—like some of the bank's paper—"Nuf sed".

The use of the pronouns of the first and second persons in the correspondence when referring to

the two banks is of no significance, such being the customary usage even between different departments of the same institution.

This correspondence when read in the light of the surrounding circumstances, carries the firm conviction that Buchholtz was saddled with the primary responsibility of covering a $50,000 overdraft and collecting between $150,000 and $200,000 of rediscounts for the Trust Company, as the Trust Company was not *"banking on the bank's endorsement anyway"* (italics ours) (Tr. 143). Naturally he was to pursue the most effective methods to accomplish this primary object. The bank must, of course, be kept afloat until he could search the note pouch and select the best available paper to cover the overdraft, and, if possible, improve the paper already rediscounted by further selection and substitution. Ellis had not been satisfactory, but "we (The Trust Company) have great confidence in your (Buchholtz) ability to pick out the kind of paper we want" (Tr. 146). Besides, keeping the bank open would induce borrowers to pay up more readily, thus insuring the collectability of the paper (Tr. 232). Also, by continuing the bank, not with the expectation of any increase in deposits, a few goodly sized out of town collection items might be transmitted for collection, which could, under appellant's contention, be well and properly applied to the payment of its account. These benefits of keeping the bank going must, of course, be had at the least possible expense. The overhead should

be reduced and the organization made efficient; and the bank must, and actually did, thereafter function primarily for the exclusive benefit of the Trust Company. Not one thought entered Buchholtz' mind concerning ways and means of restoring public confidence and building up a good will or future business for the institution. The only interest expressed by him in its continued existence was in terms of benefit to the Trust Company. In his criticism of the management he shows where his interest lies when he says the Central Bank,

> "instead of being in its present shape ought to be buying commercial paper and keep you (Trust Company) busy supplying it * * * . But there is no use crying about spilt milk" (Tr. 153-154).

To say the least, in the proper and efficient performance of Buchholtz' admitted agency for the Trust Company in the collection of rediscounts, he was expected and required to take an active interest in the conduct of all the bank's business transactions in order that the Trust Company's interests might not be adversely affected. Knowledge acquired by him in the course of such duties must be imputed to his principal, the Trust Company.

The information of Buchholtz concerning the affairs of the Central Bank was thorough and need not be detailed here. The Trust Company through him acquired a knowledge of the transactions of the bank seldom accorded a creditor in relation to the affairs of its debtor, and thus knew full well that it was continuing the business of a hopelessly

insolvent debtor bank when it appropriated the proceeds of plaintiff's check.

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13. Knowledge of Central Bank's Insolvency Communicated to Spokane.

The Trust Company was, moreover, charged with complete knowledge of the Central Bank's insolvency through its president and vice-president in charge of country banks. The letters of Buchholtz to the president (Tr. 148, 227), and his reply (Tr. 53), show a clear understanding and appreciation of the actual state of affairs, and the heavy task imposed upon Buchholtz, when shortly after his arrival at Yakima, he admonished him to "keep your head up and tail over the dash board and pray for strength".

That portion of the correspondence with the vice-president concerning the quality and value of the bank's paper has already been summarized. It does, however, contain further information of the bank's insolvency. In the letter of January 17th (Tr. 182) Triplett is fully advised of the absence of a cash reserve in the following language: "Our actual cash reserve has been running from 6% to 10%; in fact scarcely more than the cash on hand in the bank, as actual collected balances, are usually an unknown animal around here, usually offset by what our books show as overdraft with you, *the*

balance of due from sundry banks consisting of uncredited apple drafts gone hay-wire" (italics ours).

The vice-president Triplett is, moreover, almost daily advised of the withdrawal deposits and the impossibility of making collections (Tr. 164, 169, 184, 195, 199, 215). In addition to these specific instances he is frequently advised that the "situation is still in a kind of deadlock". The correspondence imparts the information embodied in the compilations on page 84 of the Transcript relating to loss of deposits and collection of notes. The Trust Company, moreover, had full knowledge of the continuous and heavy overdraft (Tr. 87), also shown on its own books, and as reported in the correspondence, and was well aware of Buchholtz' failure to cover same with rediscounts although expressly instructed to do so.

With this complete information at hand, the true condition of affairs could not be misunderstood; a banker of Mr. Triplett's experience would not fail to draw the correct conclusion from the facts in hand. But the matter was not left for inference. On the day plaintiff's check was collected and the proceeds forwarded to the Trust Company, Buchholtz unequivocally advised him that the bank was so hopelessly insolvent that it could no longer function. He says:

> "Mr. Rutter has written to me that we can expect no increase in deposits and that the only way of liquidating the indebtedness of this bank is to collect on loans. At present practically all of the paper which I have nerve enough to send for rediscount is there, with

> the exception of a small amount in the process of collection or renewal and some miscellaneous small stuff on which we haven't the statements and information. * * * If anything substantial is accomplished (by way of collection), the best grade of paper will steadily disappear with the money going out resulting in no betterment of our reserve condition. * * * This is practically the last breath. * * * I know that you have to stretch your imagination and use a high powered microscope in looking at the favorable points of the situation. In fact, compare this institution to a man at the point of death, but with a hopeful doctor on the case who is able to detect a slight heart action" (Letter, January 21, Tr. 219).

Appellant characterizes the last remark as semi-jocose. The only attempted jocularity is in the remark that the doctor should tell the family the chances of recovery were good.

Appellant attempts to find a further ray of hope in advices from Buchholtz in this letter and another letter to Mr. Rutter of the same date (Tr. 222) to the effect that the other Yakima bankers expect "a good washing out of stuff during the next ninety days", and that there would be a chance to liquidate to the extent of more than $150,000 within that period. A cursory reading of these statements in the light of the well understood facts shows that this expectation could, if realized, in no way whatsoever aid the bank or prevent its closing. All its liquid paper belonged to the Trust Company and the National City Bank of Seattle through rediscounts; $31,000 in the hands of the National City Bank

(Tr. 89), $192,000 with the Trust Company (Tr. 85), and a further $30,000 pledged with the Trust Company its collateral to the $20,000 bills payable (Tr. 137-138, statute permitting pledge of 150% of face value), making a total of approximately $250,000 outstanding and from which the Central Bank could not possibly receive any return even if collected in full. The bank had already received and expended the proceeds of this paper. Instead of constituting an asset or possible aid to the bank, this paper carried a contingent liability for the whole amount and a fixed liability on all uncollectable items. Hence, even if a large part of this paper could have been liquidated, the bank would still face a liability from that source. Thus it appears that when Buchholtz addressed himself to this feature of the situation he was merely advising his principal, the Trust Company, what to expect of him, its *"prize man"* (Tr. 104), and trusted agent in the performance of "by far the most stupendous task you have ever seen fit to put me to". In confirmation of this Buchholtz encloses a list of loans to Mr. Rutter and states that a report on the subject to him and Mr. Tripplett is in the course of preparation.

The suggestion that the National City Bank of Seattle could be induced to release its securities and accept collateral which the Trust Company itself refused to take should be, and, as appears of record, was dismissed as idle talk. Instead of attempting such a thing we find Barghoorn prior to the closing

of the bank wiring "Herb" of the National City, advising him to hold surplus liberties to secure rediscounts and to "*protect* your interests" (italics ours) (Tr. 47).

So, here, on this 21st day of January, we find the Trust Company, and each and all of its representatives connected with the transaction were well aware of the fact that the last ray of hope for the Central Bank had gone glimmering and that further effort was futile, as is confirmed by the fact that all effort to provide further funds was then and there discontinued. Not a single new rediscount was attempted or even considered (Compilation Tr. 85; rediscounts constant at $192,000 until reduced January 25th). Nothing more but substitutions and renewals for the Trust Company. Notwithstanding any consolation talk, the "Doctor" had as a matter of fact ceased all further medication.

It remains to consider the letter of Mr. Buchholtz to Mr. Rutter, dated January 23rd, in which he renders a full report and complete analysis of the situation as of Friday Night, the 21st. To begin with he says: "The last three days, I have felt very discouraged". There had been no material change in the bank's condition within that period. He then turns his attention to the subject of deposits advising that from his arrival at Yakima on the 5th "deposits dropped from $482,000 to $430,000 Friday night" (January 21st). As against this loss he reports that during his seventeen days presence with the bank "we have collected a cash

total of $15,259.08 and the enclosed adding machine slip will indicate that about $10,000 of this consisted of small items and that very little large amounts have come in and I don't expect anything large for ten days more", thus revealing an average daily collection of less than $1000.00 from a total of more than $550,000.00 bills receivable (Tr. 96), a most discouraging showing for one of our "right hand men" who had been repeatedly urged and instructed to liquidate to the limit. Thus it is obvious that none of the paper was liquid and that the best of it had become slow; but that is not the worst of it, continuing, "the large items when they do come in will, of course, go on rediscounts with no improvements in our reserve", hence providing no relief for the bank. And to show that his discouragement is not sudden, but a wearing of the "paralytic circumstances", he further says "the past week the shrinkage (of deposits) has not been bad and all of a regular nature". Referring to his efforts to cover the overdrafts it is said "I am making every effort to better that condition and as stated am nearly at the end of the rope unless one or two things can be done", and then suggests the release of Liberty Bonds in Seattle and the rediscounting of $16,000.00 worth of Barghoorn's notes with Trust Company and that if neither of these arrangements is possible

> "there is only one more avenue of relief and that is to whip up some of the stuff you are holding as collateral into rediscount and substitute a poorer class of security. * * * In

> fact, it sifts itself down to whether you desire by all means to keep this institution open * * * depending more or less on Mr. Barghoorn's personal credit, or whether you have set a limit as to how far you will go".

Neither of the modes of relief suggested were within the realm of possibility. He then states the grim necessities of the immediate future if the bank is to be kept open and declares the bank's paper will continue to deteriorate enormously. He then turns to the other side of the situation and discusses the value of the bank as an institution for future business and "earning power to charge off *bad paper*". Here we have a direct written acknowledgment of the one fact which appellant says was not known in relation to the bank's insolvency.

He then continues by pointing out how with proper management of the bank the indebtedness of the Trust Company could eventually be worked out to within reasonable bounds and made into a valuable account. After referring to the draft covering proceeds of plaintiff's check he finishes with the postscript that a further advance of $50,000 would keep the bank open and would in his "positive opinion result in a much shorter time for the Trust Company to get their money back than to close it up".

These remarks do not, as appellant contends, show any faith in the solvency of the bank; on the contrary such insolvency is fully stated and frankly

confessed. Buchholtz is merely urging Rutter to finish what he started when he came to Yakima, that is, to continue the bank regardless of solvency as the lesser of two evils. Although "discouraged" and suffering from the suspense of "waiting for something to move and bring in cash"; although it is "by far the most stupendous task you have ever seen fit to put me to; I appreciate your confidence and am not weakening". In other words, Buchholtz was still game if Rutter wanted to go the limit.

Appellant's brief seeks to brighten this utter financial darkness with four little beams of hope (Brief 84). "The proposed sale", which appellant, not then but now, takes so seriously to justify withholding plaintiff's money. Just how a transfer of stock would better the financial condition of the bank is not made plain, except upon the theory that the Trust Company could use new depositors' money to square its accounts instead of being compelled to resort to a mere collection item, and that this was the theory is so stated by Buchholtz (Tr. page 190), always looking out for the Trust Company. Next, "The expected crop movement of February and March". With all the slow and liquid paper, if any, in the Trust Company's hands, the crop movement was of no interest to the bank. Next, "A promised (by whom?) deposit of $50,000 of county funds in February". Not a chance, because Section 5563, Remington Comp. Statutes requires a deposit of good collateral, as everybody well knew.

Finally "The continued assistance of the Trust Company". Generous to a fault when dealing with country banks (Brief I, p. 9), but not quite an eleemosynary institution in its respect for collection items. No such hopes were seriously entertained. Thus do we conclude, from all the foregoing that on and before the 21st day of January, 1921, the Central Bank was well and fully aware of its hopeless insolvency through both Ellis, its official cashier and Buchholtz, its actual manager in full and complete control that the Trust Company was on and before the following day fully informed of such insolvency through the knowledge of its agent Buchholtz and the knowledge of its president and vice-president, and that as a result appellant is precluded from successfully disputing plaintiff's title to the proceeds of collection here involved. We shall, therefore, next consider whether appellant received such proceeds with knowledge of plaintiff's rights.

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14. Appellant Received the Proceeds of Collection With Full Knowledge of Plaintiff's Rights.

The proofs on this point are clear and convincing. Plaintiff's check was deposited in Seattle on the 19th and undoubtedly reached the Central Bank at Yakima on the 20th, too late for the clearings, which were closed during the morning, and consequently was held until the morning of the 21st (Tr. 35, 36). Buchholtz saw the cash letter from Seattle also

plaintiff's check and discussed the matter with Ellis. It was the practice for him and Ellis to consult each other concerning both the incoming and outgoing cash items and clearings. The letter was discussed in the usual manner and probably more at length owing to its unusual size (Ellis Tr. 96). He also discussed the cash letter and plaintiff's check with Lemon, assistant cashier (Tr. 81). On the day the bank closed Buchholtz told the witness Miner that he had handled plaintiff's check himself (Tr. 72). Buchholtz denies having seen the cash letter but admits on cross-examination that Lemon explained the matter to him (Tr. 135). On January 23rd Buchholtz wrote Rutter saying, "Yesterday we mailed a $51,000 draft on you to the Seattle National Bank covering a large letter of *items on other local banks,* the net of which has been remitted to you" (italics ours) (Tr. 231). Unquestionably Buchholtz acquainted himself with this transaction in all its details. Obviously he saw the cash letter requesting collection and *returns,* and likewise saw and remembered that it contained plaintiff's check drawn on another local bank. He says himself that he saw the draft register and from this of course was well aware of the fact that the matter was being treated as a cash and not a *credit* transaction. So much for the knowledge of Buchholtz and Rutter. What about Triplett?

As to Triplett's knowledge, the witness Miner testifies that Buchholtz told him that he had discussed the cash remittance letter and draft with

the Trust Company over the telephone and had likewise informed the Trust Company that the cash remittance made to it on the 21st by the Central Bank was the proceeds of such collection (Tr. 72-73). In confirmation of this testimony the telephone records at Yakima were produced showing a call from Buchholtz to Triplett and a twelve minute conversation on the 20th, the day plaintiff's check arrived at the Central Bank. Again on the 22nd, the day the proceeds of collection and Buchholtz' letter of the 21st arrived at the Trust Company, Triplett called and talked to Buchholtz. Triplett admits actual knowledge of the remittance on Monday morning, January 24th, when he inspected the ledger showing receipt of the $48,000 on Saturday, the 22nd (Tr. 111), but insists that he had absolutely no further knowledge on the subject at that time, and was first fully advised on the 25th. He does, however, have before him, first, Buchholtz' letter of the 21st telling him the bank is wholly without cash and begging to "hold what few pennies we might collect on your collateral notes" (Tr. 221), and, second, his own bank ledger telling him that on the same day this letter was written the bank had remitted the large round sum of $48,000. He insists that these two absolutely contradictory facts constituted the sum total of his knowledge on the subject. If such be the truth, he must have been in a great state of mental uncertainty as to whether to believe his friend Buchholtz or the figures in the ledger. Yet he would have us believe that he did

not then attempt to clear up the situation and that he did not wake up to the fact that the $48,000 did not belong to the bank until he received Buchholtz' letter referring to "*that* big draft" (Tr. 232). It is difficult to believe that he went through the day in any such state of mind. Like any other intelligent banker, he would not have acted without a clear understanding of the facts. He undoubtedly knew the true state of affairs from the beginning. He went by the ledger on his way to the executive meeting merely to check up the balance on hand that morning, in order that there might be no guess work in the discussion of the matter there. As a result of that discussion he immediately replied to Buchholtz' letter advising him that "our executive committee feel that you should *immediately* get in touch with Herb" (Tr. 225), for the purpose of providing sufficient funds to enable the bank to take its "last breath" (Tr. 221.) With the $48,000 remittance fresh in mind he further answers Buchholtz, without the slightest reference thereto, telling him quite plainly that the Central Bank cannot have those few pennies which might be collected; "we don't want to get into the position where we will ultimately lose anything". "The deal for the sale of the bank should be hurried along as fast as possible, so that our mutual friend, Mr. Barghoorn will get out without greater loss than he will now sustain"; in other words, get out from under and let the other fellow hold the bag; "If conditions go on much longer as they are now the institution

will soon be in a place where no one will purchase and then it is a case of either closing its doors or getting someone to see it through". Thus does he write without a single reference or question as to the ownership of the large remittance, and does so obviously not from indifference or lack of interest but for the apparent reason that he is then fully advised of the true nature of the remittance. Inquiry was unnecessary; he was in full possession of all the facts. The telephone had served its purpose.

Triplett admits the bank's affairs were discussed over the telephone; "he kept us informed by letter and telephone"; but denies discussion of this matter, saying, "we would not discuss any important matters over the phone which might get to the public and be detrimental to the bank"; "matters of importance that we did not object to anyone hearing would be discussed over the telephone" (Tr. 113-114). It is not quite clear how the information concerning the collection of plaintiff's check, standing alone, would be detrimental to the Central Bank. It could not possibly be so, unless such discussion should unfold a purpose to dishonor the draft. The letters, moreover, contradict him again, for instance, it is written "I tried to call you tonight but couldn't get you. Nothing in particular only I was anxious to know what had been done on the Liberty Bond matter and substitution of notes as collateral; also to give you the news of our raise in deposits today of $13,000 with $9000 in clearings for morning" (Tr. 154). Also, in a letter

to Mr. Rutter, on January 9th, three days after Buchholtz's arrival he writes, *"As already advised,* we all feel that the withdrawals have terminated" (Tr. 146). The letters show no such prior communication, calling for the conclusion that the matter was discussed by telephone.

Whatever may be the fact in this connection, the record shows conclusively that Triplett acted throughout the day on the assumption that the remittance did not belong to the Central Bank. Hence, the source of his information is not really material. The point is that Triplett knew the $48,000 had been remitted for a particular purpose and that the Central Bank had no right to use it except for that particular purpose, else it would not have been begging for pennies to keep it going.

Mr. Rutter says that he did not receive Buchholtz's letter of the 23rd until the morning of the 25th. That letter was written on Sunday and it is a singular thing that this particular letter should have been so delayed and not received until after the $45,000 draft had been presented and paid at Tacoma.

Thus, the record shows that the Trust Company, through its agent, Buchholtz, its vice president, Triplett, and its president, Rutter, was in actual touch with the collection of plaintiff's check from the time it reached the hands of the Central Bank until it dishonored the draft. Full knowledge was completely established.

Facts much less convincing than those in suit have supported a recovery. *Union Stockyards National Bank v. Gillespie,* 137 U. S. 411. There the bank was held to have notice of the plaintiff's rights to money deposited by an insolvent factor on far less conclusive testimony than that presented here. We invite the court's special attention to this case, because it is, in our opinion, conclusive.

See also,

Grandison v. First National Bank of Commerce, 231 Fed. 800;

Union Stockyards National Bank v. Moore, 79 Fed. (8th C. C. A.) 705;

Arnold v. San Ramon Bank, 194 Pac. (Cal.) 1012; 13 A. L. R. 320.

We call particular attention to the annotation of this case in the volume last cited, and especially to Subdivision IV, page 334, where the authorities are reviewed at length;

The dual agency of Buchholtz does not affect or limit the Trust Company's knowledge;

Bassett v. Evans, 253 Fed. 532. (This was a case of dual agency somewhat like the case at bar.)

Bergenthal v. Security State Bank, 112 N. W. 892. (This also is a case where an agent was acting in dual capacity).

15. The Proceeds of Plaintiff's Check Were Fully Identified and Traced into the Hands of the Defendant Trust Company.

The facts are these: Upon the receipt of plaintiff's check the Central Bank presented it for collection by its clearing agent, the Yakima Valley Bank, through the clearing house. It presented at the same time the other collection items which it had received from the Seattle National Bank, along with plaintiff's check with like instructions, amounting to $51,000. It also delivered at the same time to its agent, the Yakima Valley Bank for clearance local checks on local banks, amounting to $7800.00, asking a total of items presented at the clearing house by the Yakima Valley Bank for the Central Bank of $59,000.00.

There was on that morning presented through the clearing house by the various other Yakima Banks items against the Central Bank amounting to $9,000.00. The balance of clearings in favor of the Central Bank was $50,000 (see testimony of Lemon, record pp. 36 and 37). It appears, therefore, that the local checks presented by the Central Bank were not sufficient in amount to offset the local checks which were presented against it, by approximately $2,000.00. As there is no evidence that the Central Bank held the $7,000.00 of checks in any trust capacity, it will be presumed, as the undoubted fact was, that it was the owner of these checks. The law, therefore, will apply that $7,000.00 toward the payment in the clearance of the $9,000.00

of checks presented against the Central Bank,—this, upon the familiar rule that a trustee will be presumed to have used his own funds in such a case, rather than the trust funds.

Raynor v. Scandinavian Amer. Bk., 210 Pac. 499, 505;

Spokane Co. v. First Natl. Bk. of Spokane, 68 Fed. 979, 981 (C. C. A. 9th Circuit);

Empire State Surety Company v. Carroll Co., 194 Fed. 593, 605;

Board of Com. v. Patterson, 149 Fed. 229, 232.

This left approximately $2000 to be paid out of the trust items of $50,000 and left $48,000.00, round numbers, of the trust fund unimpaired. The Central Bank received from the Valley Bank $48,000 in the form of two drafts, leaving a small balance with the Valley Bank. These two drafts were transmitted to the Trust Company, collected, and the proceeds retained. The identification and tracing is perfect. Buchholtz in his letter to Rutter had no difficulty in making the identification. In speaking of the items including plaintiff's check he says, "The net of which has been remitted to you" (Tr. 231).

The amount of plaintiff's check was approximately $48,000, and the amount received in drafts by the Central Bank was also $48,000, but the whole amount of the trust items presented by the Central Bank was approximately $51,000.00, $3000.00, or 1/17th of which was lost in the clearings. Thus plaintiff thereby lost 1/17th of the total amount of its check and for that reason was entitled to a judgment for

only 16/17ths of the total amount of its check and judgment for that amount was entered accordingly.

The identification and tracing of the trust funds in suit is held sufficient by the following authorities:

Cragie v. Hadley, 99 N. Y. 131. (This case is cited with approval by the Supreme Court of Washington in the *Blake* case, 12 Wash. 619, cited by the appellant).

Foster v. Klinker, 35 Pac. Rep. 470 (Wyo.);

Raynor v. Scandinavian American Bank, 210 Pac. Rep. (Wash.) 499.

It is claimed by the defendant, the Trust Company, that it is incumbent upon the plaintiff to show that the funds in the hands of the trustee were augmented, and cites a number of authorities in support of its contention.

The question of augmentation arises only in cases where the plaintiff is seeking to establish a preference as against general creditors by impressing a trust upon the general funds of a receiver of an insolvent concern. The question therefore does not even arise in the case at bar, for the plaintiff is not seeking to establish a trust upon the funds in the hands of the receiver of the insolvent bank. The funds that we are seeking to reach did not come into the possession of the receiver. They had been transmitted to the defendant Trust Company before the receiver took charge.

But if such proceeds had come into the hands of the receiver they would have augumented the funds

in his hands and the plaintiff could have pursued them. The requirement that it must be shown that the assets coming into the hands of the receiver were augmented by the claimed trust funds, means nothing more than that it must be proved that he received the trust funds. The fact that the receiver would be liable in an action of debt to pay the plaintiff's claim if the trust relation was waived, does not alter the fact that the funds in the receiver's hands were augmented. It is only necessary to show that the gross assets in the hands of the receiver, not the net assets, have been augmented. The appellant's argument on this point is so fully and satisfactorily answered in the *Raynor* case (210 Pac. Rep. 499) that it is not necessary to cite further authority.

In that case the Supreme Court of Washington flatly overruled the *Spiropolas* case so strongly relied upon by the appellant in so far as the latter case held to the contrary. This point is fully covered also by the authorities cited under section 6 of this argument.

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16. Appellant's Lack of Good Faith.

The appellant makes an extended argument from pages 9 to 39 of its brief complaining of the announcement by the court set out on page 10 of the brief, wherein the trial court stated that under the circumstances disclosed by this record one bank ought not to be permitted to nurse another along until it finds a favorable opportunity to seize the money of some innocent third party to square its ac-

counts and then abandon its nursling to the tender mercies of the Bank Examiners and receivers; that such a course is forbidden by sound law and good morals. The trial court saw and heard the witnesses. He announced in his memorandum report that the proofs sustained all the allegations of complaint, except in one respect, i. e., that the plaintiff was entitled to recover the full amount (Record page 20). That he correctly characterized the conduct of the Trust Company, is fully sustained by this record. It must all be read with care to be fully appreciated. But the conduct of the Trust Company, its objects and its purposes, are fairly indicated by Triplett himself in his letter to Buchholtz written on the very day that the Central Bank received our check, when he said that Buchholtz should devote himself to the business "of *non-borrowers who will have crops and whose deposits can be used to liquidate indebtedness*" (italics ours) (Record p. 213).

After hearing and seeing the witnesses and reading the correspondence, the trial Judge could not come to any other conclusion.

The judgment of the trial court should be affirmed.

Dated, San Francisco,
May 7, 1923.

Respectfully submitted,
WALTER SHELTON,
JOHN H. POWELL,
PETERS & POWELL,
Solicitors for Appellee.